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Two Bites at the Apple: The Prejudicial Burden in Arbitration Waiver

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TABLE OF CONTENTS

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I. INTRODUCTION

Arbitration has ancient roots.[1] Disputants have long viewed arbitration as an attractive alternative to litigation.[2] In the years following the passage of the 1925 Federal Arbitration Law (FAA), commentators trumpeted arbitration's efficiencies to encourage acceptance of the FAA.[3] The judicial climate of 1925 lent an air of relevance to these commentators' arguments in favor of the new federal regime,[4] which put arbitration clauses on par with other contract clauses.[5] Before 1925, common-law precedent prohibited courts from enforcing executory agreements to arbitrate against parties who wished to revoke an arbitrator's authority.[6] This common-law holdover badly weakened the institution of

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[1] *See* Sabra A. Jones, *Historical Development of Commercial Arbitration in the United States*, 12 MINN. L. REV. 240, 242–43 (1928) (locating arbitration in the classics); Paul L. Sayre, *Development of Commercial Arbitration Law*, 37 YALE L.J. 595, 597 (1928) ("There was a partially developed system of arbitration in Roman law, both during the classical period and under Justinian.").

[2] *See* Jones, *supra* note 1, at 243 ("What is arbitration like? Gentle, fair . . . ." (internal quotation marks omitted) (quoting Cicero)).

[3] *See* Julius H. Cohen & Kenneth Dayton, *The New Federal Arbitration Law*, 12 VA. L. REV. 265, 269 (1926) (enumerating three "evils which arbitration is intended to correct": court congestion, litigation expense, and judges' lack of business expertise); Jones, *supra* note 1, at 240 (lamenting judges' unfamiliarity with trade practices and the inexperience of juries compared to arbitrators).

[4] *See* Part II *infra*.

[5] *See* 9 U.S.C. § 2 (2017) (making agreements to arbitrate irrevocable "save upon such grounds as exist at law or in equity for the revocation of any contract"); *see also* H.R. REP. NO. 68-96, at 1 (1924) ("An arbitration agreement is placed upon the same footing as other contracts, where it belongs.").

[6] *See* Red Cross Line v. Atl. Fruit Co., 264 U.S. 109, 120–21 (1924) ("The federal courts—like those of the states and of England—have, both in equity and at law, denied, in large measure, the aid of their processes to those seeking to enforce executory agreements to arbitrate disputes."). This was true despite the courts' professed misgivings. *See, e.g.*, Berkovitz v. Arbib & Houlberg, Inc., 130 N.E. 288, 292 (N.Y. 1921) (opinion of Cardozo, J.) ("The ancient rule, with its exceptions and refinements, was criticized by many judges as anomalous and unjust. It was followed with frequent protest to early precedents."); Kulukundis Shipping Co. v. Amtorg Trading Corp., 126 F.2d 978, 983–84 (2d Cir. 1942) (noting that lower courts, feeling bound to comply with precedent, nevertheless became critical of judicial hostility to arbitration).

arbitration—an institution that academics,[7] legislators,[8] and even judges[9] agreed would aid dispute resolution in the United States.

With the courts unwilling to reverse precedent, legislatures stepped in to make arbitration agreements enforceable.[10] The states were first to act,[11] but Congress followed soon after, passing the FAA in 1925. Now it was the courts' job to apply the law with regularity so that the acclaimed benefits of arbitration would inure to the American legal system.[12] The body of law that then emerged gave life to what the Supreme Court would call the "liberal federal policy favoring arbitration agreements."[13] This policy means that courts liberally enforce arbitration agreements to advance the cost-saving policy goals of the FAA.[14]

What began as a countermeasure to judges' historical hostility[15]—a countermeasure that aimed to place arbitration "upon the same footing as other contracts"[16]—grew over the following decades into a strong federal policy that judges invoked when they enforced agreements to arbitrate.[17] Even now, courts often use this

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[7] *See* Jones, *supra* note 1, at 240 (stating the purposes of arbitration as eliminating the expense of litigation, saving delays in legal proceedings, improving business relations between industry people and customers, establishing trade customs, and substituting the decisions of practical business men for those of inexperienced juries); Cohen & Dayton, *supra* note 3, at 265 ("The movement finds its origin in the unfortunate congestion of the courts and in the delay, expense and technicality of litigation."); *see also* Sayre, *supra* note 1, at 615 ("Business men want arbitration which gives them experts to pass upon the facts, which are often far more important than questions of law involved in commercial suits.").

[8] H.R. REP. NO. 68-96, at 2 (1924).

[9] *See* Jones, *supra* note 1, at 256 (noting that American courts believed "the policy of arbitration was wise and should be encouraged" but that "it was the duty" of the legislature to pass a law favoring enforcement).

[10] *Id.*

[11] *Id.* at 247–48 (observing that before 1920 several states had made agreements to arbitrate irrevocable); *see also id.* at 261 (observing the trend from 1920 of adopting "a uniform state statute where submission is irrevocable").

[12] *See, e.g.*, Kulukundis Shipping Co. v. Amtorg Trading Corp., 126 F.2d 978, 985 (2d Cir. 1942) ("In light of the clear intention of Congress, it is our obligation to shake off the old judicial hostility to arbitration.").

[13] Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 24 (1983).

[14] *Id.*

[15] *See* H.R. REP. NO. 68-96, at 1 (1924) ("The need for the law arises from an anachronism of our American law."); Jones, *supra* note 1, at 256 ("In the early history of the United States there was considerable objection to arbitration.")

[16] H.R. REP. NO. 68-96, at 1 (1924).

[17] *See, e.g.*, Collado v. J. & G. Transp., Inc., 820 F.3d 1256, 1259 (11th Cir. 2016) ("Federal policy strongly favors enforcing arbitration agreements." (internal citations omitted)); Banc One Acceptance Corp. v. Hill, 367 F.3d 426, 429 (5th Cir. 2004) ("[O]nce a court determines

policy to save costs, free up dockets, and call on expert decision makers.[18]

But courts' application of the federal policy favoring arbitration has caused inefficiencies, encouraging the kind of spending and delay that arbitration instead ought to prevent.[19] These inefficiencies crop up perennially in the context of arbitration waiver. A party resisting arbitration based on the other party's alleged waiver must show that the waiving party acted as though it intended to litigate, not arbitrate.[20] This is true in arbitration waiver as it is in any contract waiver situation.[21] All circuits require at least this showing, but most require more.[22]

Most circuits have ruled that a party resisting a motion to compel arbitration must prove (1) that the movant acted inconsistently with its right to arbitrate and (2) that the movant's inconsistent acts caused the nonmovant prejudice.[23] Courts that maintain this rule place the burden on the nonmovant to show prejudice.[24] Even if the party moving to compel arbitration has broadcasted its plans to litigate through its overt acts, those acts may not amount to a waiver absent a showing that those acts prejudiced the nonmoving

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that an agreement to arbitrate exists, the court must pay careful attention to the strong federal policy favoring arbitration and must resolve all ambiguities in favor of arbitration." (internal citations omitted)).

[18] *See* Jones, *supra* note 1, at 240 (listing the purposes of arbitration).

[19] *See* E. C. Ernst, Inc. v. Manhattan Const. Co. of Texas, 559 F.2d 268, 269 (5th Cir. 1977) (finding that a party's delay in invoking arbitration caused the nonmovant to bear the type of expenses that arbitration was designed to avoid).

[20] *See, e.g.*, Lewallen v. Green Tree Servicing, L.L.C., 487 F.3d 1085, 1090 (8th Cir. 2007) (finding that a party waived its arbitral rights where it acted inconsistently with the right to arbitrate); St. Mary's Med. Ctr. of Evansville, Inc. v. Disco Aluminum Prod. Co., 969 F.2d 585, 588 (7th Cir. 1992) ("The essential question is whether, based on the circumstances, the alleged defaulting party has acted inconsistently with the right to arbitrate.").

[21] 13 WILLISTON ON CONTRACTS § 39:22 (4th ed.) ("Waiver, as an excuse for nonperformance of a contract, is essentially a matter of intention.").

[22] *See infra* Part III.

[23] *See, e.g.*, LG Elecs., Inc. v. Wi-Lan USA, Inc., 623 Fed. Appx. 568, 569 (2d Cir. 2015) ("[W]aiver 'may be found only when prejudice to the other party is demonstrated.'" (quoting Thyssen, Inc. v. Calypso Shipping Corp., 310 F.3d 102, 105 (2d Cir. 2002))); Joca-Roca Real Estate, LLC v. Brennan, 772 F.3d 945, 948 (1st Cir. 2014) ("[M]ere delay in seeking [arbitration] without some resultant prejudice is insufficient to ground a finding of conduct-based waiver." (second alteration in original) (quoting Creative Solutions Grp., Inc. v. Pentzer Corp., 252 F.3d 28, 32 (1st Cir. 2001))).

[24] *See Joca-Roca Real Estate*, 772 F.3d at 948 ("The party advocating waiver has the burden of demonstrating prejudice.").

party.[25] Acts that would ordinarily show a party's intent to litigate include delaying before invoking its right to arbitrate, choosing a litigation venue or removing to a different litigation venue, undertaking preliminary motions practice, filing dispositive motions, collaborating with the court and the other party in pretrial meetings, or engaging in discovery.[26]

So the burden of prejudice may allow, and even encourage, litigants to create the very costs that Congress introduced the FAA to save. A party may use arbitration as a "plan B" as soon as its litigation strategy has gone awry, or as soon as the party has won some advantage through litigation that it might not have won in arbitration. The burden of prejudice paves the way for a strategy that Judge Posner has called, "[H]eads I win, tails you lose."[27]

Given how litigants have manipulated the rules that require a showing of prejudice, this Note advocates for a different rule: courts should find that a party has waived its right to arbitrate when the party undermines the purposes of the FAA by wastefully litigating before moving to arbitrate. The Seventh Circuit has held that a party's decision to proceed with a suit in court raises a rebuttable presumption that the party has waived its right to arbitrate.[28] This presumption has the virtue of eliminating the prejudice requirement, but does not squarely address the problems of duplicative litigation and gaming the system by trying two venues. Instead, courts should adopt a rule that is both broader and narrower than the Seventh Circuit's presumption. It is true that a bright-line presumption of waiver when parties fail to raise arbitration as a defense has the benefit of clarity. However, the trigger for this presumption (failure to raise an arbitration defense in an answer) is too mechanical and may encourage courts to find

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[25] *See, e.g.*, Patten Grading & Paving, Inc. v. Skanska USA Bldg., Inc., 380 F.3d 200, 208 (4th Cir. 2004) (requiring more than the legal expenses inherent in litigation to show prejudice). For a full discussion of the activity that might lead a court to find waiver, see Donald E. Frechette, *Waiving the Right to Arbitrate by Participating in Litigation*, 80 DEF. COUNSEL J. 223 (2013).

[26] *See* Frechette, *supra* note 25, at 224–229.

[27] Cabinetree of Wis., Inc. v. Kraftmaid Cabinetry, Inc., 50 F.3d 388, 391 (7th Cir. 1995).

[28] *Id.* at 390; *see also* Lilly, *supra* note 145, at 109 . *But see* Kawasaki Heavy Indus., Ltd. v. Bombardier Recreational Prods., Inc., 660 F.3d 988, 995 (7th Cir. 2011) (holding that a party does not waive its right to arbitrate by filing a motion to dismiss (citing Faulkenberg v. CB Tax Franchise Sys., LP, 637 F.3d 801, 807 (7th Cir. 2011))).

waiver where the party's failure was justified and the parties (and society as a whole) might still save time and money by arbitrating.

Instead, courts should apply a two-tiered analysis in finding arbitration waiver. Under the first tier, courts should automatically find waiver if a party deliberately manipulates the judicial process to gain a tactical advantage or gains an advantage it would not have gained in arbitration. For example, a party might win a smoking-gun document in a discovery dispute, which it would not have won in arbitration's less-probing fact-finding process. That would should lead to automatic waiver.

Under the second, less-demanding tier, courts should rebuttably presume waiver where a party duplicates the machinery of arbitration by litigating in court. This rule would prevent most duplicative litigation while allowing an equitable outlet for parties that pursued litigation in good faith.[29] A party's good-faith decision to litigate, rather than arbitrate, is a lesser evil than a deliberate manipulation of the courts to gain a tactical advantage. But invoking arbitration after extensive pretrial proceedings is still wasteful and should raise a rebuttable presumption of waiver. [30]

Part II of this Note traces the history of arbitration from its roots, focusing on its development in the English common law and its transfer to American courts. This survey will clarify the context in which Congress passed the FAA in 1925, the challenges that Congress sought to address, and the benefits that Congress hoped to provide. Part II will show how courts readily adopted and applied the FAA, but also how courts became overzealous in their application of the FAA. Part III will discuss the problematic overextension of the policy favoring arbitration in the arbitration waiver context. It will examine the prevailing rule among circuits,

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[29] A case might arise where a party has not yet determined the scope of arbitrability for a given issue, but they are running up against a statute of limitations. *See infra* note 183 and accompanying text. Courts have also excused failure to invoke arbitration in a timely manner when invocation would have been futile (because the law changed during the party's delay), *see* Chassen v. Fidelity Nat'l Fin., Inc., 836 F.3d 291, 299 (3d Cir. 2016) (excusing delay where mortgagors' initial motion would have failed before a change in law), and when some major change occurred in the course of litigation that substantially altered the parties' positions, *see* United States v. Cyberonics, Inc., 146 F. Supp. 3d 337, 350 (D. Mass. 2015) (no waiver where party delayed to file motion to dismiss non-arbitrable claims).

[30] *See* Gray Holdco, Inc. v. Cassady, 654 F.3d 444, 454 (3d Cir. 2011) ("[A] party may not use arbitration to manipulate the legal process and in that process waste scarce judicial resources.").

under which a party resisting a motion to compel arbitration must show that the movant's actions caused it prejudice. Finally, Part IV will advocate a two-tiered waiver rule that prevents duplicative litigation and strategies that abuse courts' ready enforcement of arbitration, while also affording parties an equitable outlet.

II. THE FAA: HISTORY AND CONTEXT

Congress devised the FAA to address a judge-made problem. On January 24, 1924, Representative George Scott Graham of Pennsylvania, speaking on behalf of the Committee on the Judiciary, described "an anachronism of our American law" that had created the need for the new legislation that he would shortly propose: the FAA.[31] The anachronistic law was judge-made; the remedy would be legislative.

This Part discusses both the judicial problem and the legislative solution. It examines the history of courts' unwillingness to enforce arbitration and legislators' efforts to correct that unwillingness. And it explains how, in response to legislators' efforts, courts erected an "edifice of [their] own creation."[32]

A. THE MYTH OF JUDICIAL JEALOUSY

Representative Graham explained that English courts' unwillingness to enforce arbitration agreements had passed into American law and embedded itself there.[33] Attempting to explain English courts' refusal to enforce agreements to arbitrate, Representative Graham cited "the jealousy of the English courts for their own jurisdiction."[34] He said that although American courts had criticized the rule and its illogicality, the rule was too strongly fixed for courts to overturn it without legislative permission.[35]

Representative Graham's history was incomplete, but his conclusion about American courts' reluctance to change was apt. The Second Circuit would later call his conjecture about judicial

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[31] H.R. REP. NO. 68-96, at 1 (1924).

[32] Allied-Bruce Terminix Cos. v. Dobson, 513 U.S. 265, 283 (1995) (O'Connor, J., concurring).

[33] H.R. REP. NO. 68-96, at 1–2 (1924).

[34] *Id.* at 1.

[35] *Id.* at 2.

jealously "quaint," a product of legal minds manufacturing a reason for a rule.[36] Other commentators agreed that this jealousy rationale was a myth.[37] Like the Second Circuit,[38] Professor Paul Sayre emphasized that the doctrine of "judicial jealousy"[39] gained judicial acceptance without even a modicum of evidentiary support.[40] The doctrine first appeared in *Kill v. Hollister* (1746), 95 Eng. Rep. 532; 1 Wils. 129, without any citation of authority.[41]

The Senate Judiciary Committee also addressed courts' unwillingness to enforce arbitration agreements.[42] But they expanded on Representative Graham's historical explanation for this unwillingness[43] by giving a comprehensive list of reasons: the fear that extrajudicial tribunals lacked the power to give full redress; the doubt that courts could compel an unwilling party to arbitrate, denying the party its right to judicial hearing and determination; courts' jealousy and their fear of ouster; and the weight of precedent.[44]

Rejecting the notion of judicial jealousy and fear of ouster as baseless,[45] Professor Sayre endorsed the procedural explanations of courts' unwillingness to compel arbitration. He traced arbitration's roots to the Classical period and suggested that arbitration came to the common law through Ecclesiastical courts.[46] Arbitration was

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[36] *See* Kulukundis Shipping Co., v. Amtorg Trading Corp., 126 F.2d 978, 983 (2d Cir. 1942) (noting that awards under arbitration, as well as releases and covenants not to sue, were no less an ouster than arbitration agreements, but courts willingly enforced them); *see also* Jones, *supra* note 1, at 258 ("Furthermore the court is not robbed of its jurisdiction for an award once made is enforceable through a judgement of the court.").

[37] *See* Sayre, *supra* note 1, at 610 (rejecting the notion of "contests of the courts of ancient times for expansion of jurisdiction" (citations omitted)). See also, with respect to modern courts, JULIUS H. COHEN, COMMERCIAL ARBITRATION AND THE LAW 260 (1918) ("In our day, there is little evidence of jealousy on the part of the courts over the disposition of controversy by private tribunals.").

[38] *See Kulukundis*, 126 F.2d at 983 ("[T]he legal mind must assign some reason in order to decide anything with spiritual quiet.").

[39] Sayre, *supra* note 1, at 609.

[40] *Id.* at 610.

[41] *Id.* at 604.

[42] *See* S. REP. NO. 68-536, at 2 (1924) (noting the "very old law" that arbitration clauses would not be enforced in equity or at law).

[43] *Id.*

[44] *Id.* at 2–3.

[45] *See* Sayre, *supra* note 1, at 610 ("It is difficult to see the justice in attributing such unworthy motives to the courts in their development of arbitration law . . . .").

[46] *Id.* at 597.

foreign to Anglo-Saxon law at that time, and the King's courts would not have favorably entertained the idea when it appeared.[47] After all, the courts were both a source of revenue for the crown and a vehicle for political consolidation.[48] Arbitration was a purely private matter with little structural support beyond the enforcement that the common law would, or would not, offer.[49] After the passage of the Statute of Fines and Penalties in 1687,[50] which capped at actual damages the recovery for breach of an arbitration agreement, the courts eventually held that they would only allow nominal damages.[51] What damage could a party suffer for the "high privilege and great advantage" of the King's courts?[52] A later law authorized parties to ask courts to make arbitration "irrevocable."[53] But given English courts' distaste for arbitration, that authorization had no teeth.[54]

Judges' aversion to arbitration likely stemmed from their desire to give parties due process.[55] English and American courts had tools to secure testimony and subpoena witnesses, as well as external guarantees of impartiality.[56] To avoid depriving parties of these

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[47] *Id.* at 597–98.

[48] *See id.* at 598 ("Perhaps the main purposes of the King's justice were political and financial, in consolidating and unifying the kingdom and in bringing fees into the royal treasury."). The idea that judges in England were unwilling to forfeit their fees featured in the rhetorical toolbox of arbitration's chief proponents. See, for example, Julius H. Cohen's preterition in a joint hearing before the House and Senate Judiciary: "Of course, some of the justices have been unkind enough to their predecessors to say that there was a time when the judges were paid according to the cases they acted upon and the fees they got. I do not want to reflect on the judiciary in that way, although there is some historical basis for believing it." *Bills to Make Valid and Enforceable Written Provisions or Agreements for Arbitration of Disputes*, 68th Cong. 1 (1924) (statement of Julius H. Cohen).

[49] Sayre, *supra* note 1, at 598 (describing how "arbitration was entirely a matter of private arrangement for which there was no authority except the personal authority of the parties to the agreement"); Jones, *supra* note 1, at 245 ("The courts of law in England held that the parties were at liberty to revoke the authority given to an arbiter, under the submission, at any time before an award was made.").

[50] 8 & 9 Will. 3 c. 11, § 8 (Eng.).

[51] Sayre, *supra* note 1, at 604.

[52] *See id.* at 604 (noting that "to recover damages because one had to try his case there was a little more than the courts could understand").

[53] *Id.* at 605.

[54] *See id.* ("[T]he act could not be used extensively, since the submission was still revocable until a rule of court enforcing it had been obtained.").

[55] *Id.* at 611 (noting that arbitration lacks the usual means of securing an impartial hearing).

[56] *Id.*

procedural rights, courts shied from enforcing executory agreements to arbitrate.[57] The risk of procedural deprivation ran higher when the parties were on unequal bargaining terms[58]—a concern that has not dissipated with time.[59]

Regardless of their reason for disfavoring arbitration, by 1924, the courts' distaste for arbitration had drawn attention at the highest level of government in the United States.[60] Both the House and Senate Judiciary Committees acknowledged it in introducing the FAA, and the Supreme Court noted it in the same year.[61] Both houses of Congress derided the "anachronism"[62]—the "ancient rules"[63]—and they sought to place arbitration on par with other agreements.[64] The fruit of their labors was, of course, the FAA.

B. THE FAA'S PURPOSE

To assess contemporary courts' application of the FAA, it is useful to understand Congress's goals in passing the Act. The reports contemporary with the FAA's consideration show the

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[57] *Id.* (describing the courts view that arbitration "involve[d] such a limitation upon the parties' fundamental rights . . . that the courts [would] not enforce [arbitration]").

[58] *Id.*; *see also id.* at 616 (noting that opponents of the FAA feared that small merchants or customers might be coerced into arbitration agreements, depriving them of their day in court).

[59] *See, e.g.*, AT&T Mobility LLC v. Concepcion, 563 U.S. 333, 343 (2011) (favoring the FAA over a California statute allowing courts to strike arbitration clauses for unconscionability, including procedural unconscionability in light of unequal bargaining power); Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 32–33 (1991) (considering and rejecting the argument that arbitration should not be enforced in ADEA contexts due to unequal bargaining).

[60] While England passed its distaste for arbitration to America through the common law, Parliament anticipated Congress in reforming the distaste when it enacted statutes in 1833 and 1889 making written agreements to arbitrate irrevocable, except by leave of the court, and expanding the procedural powers of arbitrators. *See supra* note 50.

[61] *See* Red Cross Line v. Atl. Fruit Co., 264 U.S. 109, 120–21 (1924) (emphasizing that English and American courts, state and federal, had denied their aid in seeking to enforce arbitration). The Bar, too, had evidently come around. *See* Jones, *supra* note 1, at 258 (noting that lawyers, finding themselves in the capacity of legal advisers to the trade associations, enjoyed the appreciation of clients who avoided the cost and delay of legal proceedings).

[62] H.R. REP. NO. 68-96, at 1 (1924).

[63] S. REP. NO. 68-536, at 2 (1924).

[64] *See* H.R. REP. NO. 68-96, at 1 (1924) ("An arbitration agreement is placed on the same footing as other contracts, where it belongs."); S. REP. NO. 68-536, at 3 (1924) ("The record made under the supervision of this society shows . . . the practical justice in the enforced arbitration disputes where written agreements for that purpose have been voluntarily and solemnly entered into.").

legislature's objective: to correct judges' reluctance to enforce arbitration agreements so that arbitration agreements would bind parties as effectively as any other freely made contract.

The reasons why Congress wanted to revitalize arbitration—to save costs, alleviate docket clogs, and inject experts into disputes—can guide courts' interpretation and application of the FAA. These three purposes can be found in two principal places: the language of the congressional reports contemporaneous with the Act's consideration, and the structure of the Act itself.

1. The Congressional Reports

The reports from the House and Senate show that the two chambers were of one mind regarding the need for legislative action to advance the cause of arbitration.[65] As explained above, their understandings of the relevant history were somewhat different, but the House's and Senate's hopes for the Act were the same.[66] The law was passed in a climate of judicial hostility to arbitration, which the legislature hoped to squelch.[67]

Both chambers predicted that the new law would reduce the expense of litigation and mitigate the delays that had come to characterize the courts, and both chambers emphasized the advantage of arbitrators' business expertise.[68] The House Report described arbitration as a way of "reducing technicality, delay, and expense to a minimum."[69] A party willing to submit a dispute to arbitration would not be subject to the "delay and cost of litigation."[70] The House deemed the Act's passage to be "practically appropriate . . . at this time when there is so much agitation against the costliness and delays of litigation. These matters can be largely

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[65] *Compare* H.R. REP. NO. 68-96 (1924) *with* S. REP. NO. 68-536 (1924).

[66] One commentator has observed that, due to the Bar Association's several years of lobbying before Congress in favor of uniform federal procedure, the members of Congress were probably familiar with problems like court clogs and delays. IMRE SZALAI, OUTSOURCING JUSTICE: THE RISE OF MODERN ARBITRATION LAW IN AMERICA 170 (2013).

[67] *See* IAN R. MACNEIL, AMERICAN ARBITRATION LAW: REFORMATION—NATIONALIZATION—INTERNATIONALIZATION 105 (1992) ("Perhaps the most important single factor in understanding congressional intention respecting the [FAA] is the legal background against which the [FAA] was presented to Congress.").

[68] *Cf.* AT&T Mobility LLC v. Concepcion, 563 U.S. 333, 345 (2011) (noting Congress's original purpose for the FAA to remediate the expense and delay of litigation).

[69] H.R. REP. NO. 68-96, at 2 (1924).

[70] *Id.*

eliminated by agreements for arbitration, if arbitration agreements are made valid and enforceable."[71]

The Senate reiterated the House's position. The Senate Judiciary Committee, reporting on the Act, observed that

> arrangements for avoiding the delay and expense of litigation and referring a dispute to friends or neutral persons are a natural practice of which traces may be found in any state of society.' The desire to avoid the delay and expense of litigation persists. The desire grows with time and as delays and expenses increase.[72]

The committee also noted "a brief résumé" from the New York Times describing the successes of the Arbitration Society of America:

> In contrast with the long time required by the courts with their congested calendars to settle a dispute, the records of the society show that the average arbitration required but a single hearing, and occupied but a few hours of the time of disputants, counsel, and witnesses. The cost to disputants was said to be trifling as compared with the cost of litigation.[73]

Both houses were preoccupied with the delay and expense of litigation, and their preoccupation was a sign of the times. Much of the delay and expense that Congress targeted with the FAA arose from the civil procedural patchwork of the early twentieth century.[74] Under the Conformity Act of 1872, federal courts were supposed to "conform, *as near as may be*, to the practice, pleadings, and forms and modes of proceeding existing at the time in like causes in the courts of record of the State within which such circuit or district courts are held."[75] This rule of conformity meant that judges and lawyers had to tackle burdensome, case-by-case determinations

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[71] *Id.*

[72] S. REP. NO. 68-536, at 3 (1924).

[73] *Id.* (quoting N.Y. TIMES, May 11, 1924).

[74] *See* SZALAI, *supra* note 66, at 167 (describing state-by-state variations).

[75] *Id.* (quoting 4 CHARLES ALAN WRIGHT & ARTHUR MILLER, FEDERAL PRACTICE AND PROCEDURE: CIVIL § 1002 (3d ed. 1998)).

about procedural rules.[76] The FAA was part of a broader effort to streamline and reform procedure in federal courts.[77] While that effort was not fully realized until 1938 when the Federal Rules of Civil Procedure took effect,[78] the FAA's passage in 1925 was a major event in this procedure-focused era.[79]

2. The Structure of the Act Itself

The core operative provision of the Arbitration Act is § 2.[80] Section 2 provides that "an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract."[81]

In arguing against a broad construction of the FAA, Ian MacNeil describes the law as "an unquestionably integrated, unitary statute, consisting of core provisions and provisions supplementing them."[82] MacNeil's structural description finds support in history: Congress lifted the key language in the statute—that written agreements to arbitrate "shall be valid, irrevocable and enforceable"[83]—directly from the relatively recent New York Arbitration Law of 1920.[84] MacNeil reasons that Congress intended to create an integral statute, like New York's, organized around the enforceability provision.[85] All other provisions in both the FAA and the New York

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[76] *See id.* at 169 ("[I]t was often recognized that [] a [uniform federal court procedure] law would simplify procedure and alleviate the frustrations and costs of the confusing, hyper-technical, uncertain procedure existing in federal courts at the time.").

[77] *See id.* at 168 ("Dissatisfaction with the existing and confusing procedures in federal court gave rise to a movement to reform federal court procedure.").

[78] *Id.* at 169 (discussing the history of efforts to unify federal court procedure).

[79] *See id.* at 170 ("All these reforms can be understood as related to the same overall push for dealing with the 'law's delays' and improving the administration of justice.").

[80] 9 U.S.C. § 2 (2012).

[81] *Id.*

[82] MACNEIL, *supra* note 67, at 105–06. MacNeil argues that the FAA was a procedural remedy designed for federal courts, not state courts. While this Note argues that courts have extended the liberal federal policy in favor of arbitration agreements too far in the arbitration waiver context, the larger, though related, question of whether the FAA applies to state courts is beyond the scope of this discussion.

[83] 9 U.S.C. § 2 (2012).

[84] MACNEIL, *supra* note 67, at 106.

[85] *Id.* at 106–07.

law depended on the validity, irrevocability, and enforceability of agreements to arbitrate.

The FAA's proponents used language that reinforced § 2's centrality. In the House, the Judiciary Committee declared that the "purpose of this bill is to make valid and enforcible agreements for arbitration."[86] And the Senate Judiciary Committee described "the bill . . . to make valid and enforceable written provisions or agreements for arbitration."[87] The Senate Judiciary Committee did not mince words when describing the substance of the law: "The purpose of the bill is clearly set forth in section 2."[88]

Taken together, the FAA's jurisprudential context, the congressional reports contemporaneous with its passage, and the centrality of § 2 together yield a narrative of congressional purpose. Congress introduced and passed the FAA in response to the sticky problem of judges' unwillingness to enforce arbitration agreements. It did so to cut down on the expense and delay of arbitration and to inject the judgment of an expert arbitrator into complex commercial disputes. To do all of that, Congress produced § 2, which placed arbitration agreements on par with other contracts.[89] Absent from the Act's history and passage was an explicit endorsement of strong federal policy in favor of arbitration. But this strong policy soon surfaced in the courts as the doctrinal bridge between the Act and its relentless application.

C. THE FAA IN THE COURTS

The staunchest critics of the strong federal policy favoring arbitration argue that judges created it.[90] They argue that this policy is divorced from the Act's history and from Congress's

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[86] H.R. REP. NO. 68-96, at 1 (1924).

[87] S. REP. NO. 68-536, at 1 (1924).

[88] *Id.* at 2.

[89] *See* Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 625 (1985) (describing § 2 as the "Act's centerpiece provision").

[90] *See, e.g.*, Allied-Bruce Terminix Cos. v. Dobson, 513 U.S. 265, 283 (1995) (O'Connor, J., concurring) (describing FAA jurisprudence as an edifice of the Court's own creation); Imre Stephen Szalai, *Exploring the Federal Arbitration Act Through the Lens of History*, 2016 J. DISP. RESOL. 115, 117 (2016) (arguing that the Supreme Court has erred in extending the FAA to disputes beyond a limited, modest system of private dispute resolution).

designs.[91] And they often argue against the Court's expansive reading of the FAA from a federalist perspective, suggesting that the Court should never have extended the FAA to cover disputes in state courts.[92]

This Note does not grapple with the Supreme Court's extension of the FAA to state court disputes or its application in areas beyond commercial disputes. But courts' role in the establishment of a strong federal policy favoring arbitration is clear.[93] American courts, which had long followed English precedent in refusing to enforce arbitration agreements,[94] faithfully implemented the Act that Congress had passed to free them from that precedent, paving the way to a more effective domestic arbitration regime.[95] The federal policy favoring arbitration bridged Congress's driving purposes for the Act (cost savings, clearing dockets, and expertise) with its application in trial courts.

However, courts have defied Congress's purposes by extending the federal policy to litigation contexts where invoking the rule undermines the core purposes of the FAA. A brief examination of the birth and development of the federal policy favoring arbitration shows that courts—first the circuits and eventually the Supreme Court—had congressional purpose in mind when they invoked the policy. But this conscientiousness dissolved in the arbitration waiver context, as courts invoked the strong federal policy to justify wasteful rules requiring prejudice as an element of waiver.[96]

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[91] *See* Circuit City Stores, Inc. v. Adams, 532 U.S. 105, 128 (2001) (Stevens, J., dissenting) (suggesting that the Supreme Court has been "[p]laying ostrich" to the substantial history behind the employment amendment of § 1 of the FAA); *Allied-Bruce*, 513 U.S. at 283 ("Yet, over the past decade, the Court has abandoned all pretense of ascertaining congressional intent with respect to the Federal Arbitration Act . . . ."); SZALAI, *supra* note 66, at 117; MACNEIL, *supra* note 67, at 146 (noting that "not one thing in the legislative history" suggests that Congress intended the FAA to apply in state courts).

[92] *See Allied-Bruce*, 513 U.S. at 282 (O'Connor, J., dissenting) ("As applied in state courts, however, the effect of a broad formulation of § 2 is more troublesome."); MACNEIL, *supra* note 67, at 135; SZALAI, *supra* note 66, at 117.

[93] *See supra* note 90.

[94] *See supra* Part II.A.

[95] Kulukundis Shipping Co. v. Amtorg Trading Corp., 126 F.2d 978, 985 (2d Cir. 1942) ("In the light of the clear intention of Congress, it is our obligation to shake off the old judicial hostility to arbitration.").

[96] *See infra* Part III.

1. The Edifice of Arbitration Policy

The Supreme Court first invoked the policy favoring arbitration in *Moses H. Cone Memorial Hospital v. Mercury Construction Corp*.[97] An Alabama contractor (Mercury) sued in district court to compel arbitration in its dispute with a North Carolina hospital (Moses H. Cone).[98] The district court stayed federal proceedings pending resolution of concurrent state court claims.[99] Mercury appealed the stay, arguing that the district court should have compelled arbitration, and the Fourth Circuit agreed.[100] The Supreme Court granted certiorari to determine whether the district court should have stayed the federal claims pending resolution of the state court claims or whether it should instead have compelled arbitration.[101]

The Supreme Court held that the district court erred in refusing to compel arbitration.[102] Among other factors weighing in favor of arbitration, the Court described a liberal federal policy in favor of arbitration,[103] which the Court located in § 2, the FAA's enforcement provision.[104] The Court cited "Congress's clear intent . . . to move the parties . . . into arbitration as quickly and easily as possible."[105] It also concluded that "[§] 2 is a congressional declaration of a liberal federal policy favoring arbitration agreements."[106] And the court noted that "the courts of appeals have since consistently concluded that questions of arbitrability must be addressed with a healthy regard for the federal policy favoring arbitration."[107]

By the time the Court was writing, roughly fifty-eight years after the FAA's enactment, a number of circuits had indeed developed a pro-arbitration policy.[108] But as *Moses H. Cone* plainly shows by its

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[97] Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 24 (1983) (describing and applying "a liberal federal policy favoring arbitration agreements" based on § 2 of the FAA).

[98] *Id.* at 4, 7.

[99] *Id.* at 8.

[100] *Id.* at 4.

[101] *Id.*

[102] *Id.* at 29.

[103] *Id.* at 24.

[104] *Id.* ("Section 2 is the primary substantive provision of the Act . . . ."). For a discussion of the centrality of this provision, see Part II.B above.

[105] *Id.* at 22.

[106] *Id.* at 24.

[107] *Id.*

[108] *See id.* at 25 n.31 (collecting cases).

strange reliance on circuit court holdings for support, this policy was not the legacy of a seminal, post-FAA Supreme Court decision. Its development was a disorderly mishmash of jurisprudence, a true legacy of common law.

Many courts in the mid-twentieth century invoked the federal policy favoring arbitration, even if they did not use those words exactly. In 1968, the First Circuit noted the "vigorous policy favoring arbitration."[109] Not long after—but before *Moses H. Cone*—the Third Circuit described arbitration as a "favored policy for the resolution of disputes."[110] In the Fourth Circuit, the policy had surfaced by 1971.[111] The Ninth Circuit described "the strong federal policy supporting international arbitration agreements" in a 1978 case.[112] And in the Eleventh Circuit, "any party arguing waiver of arbitration [bore] a heavy burden of proof" in 1978.[113]

Post-*Moses H. Cone* courts tended to cite the Supreme Court to support their endorsement of the strong federal policy favoring arbitration.[114] But before *Moses H. Cone*, the courts had to look elsewhere. By and large, the circuits drew support for the policy favoring arbitration from a common source: the Second Circuit's decisions in *Kulukundis* and *Carcich.*[115]

Kulukundis was the earliest case to explicitly describe the federal policy favoring arbitration.[116] Decided 15 years after the FAA's enactment, *Kulukundis* demonstrated a new, pro-arbitration

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[109] Hilti, Inc. v. Oldach, 392 F.2d 368, 371 (1st Cir. 1968) (citing Galt v. Libbey-Owens-Ford Glass Co., 376 F.2d 711, 714 (7th Cir. 1967) and Robert Lawrence Co. v. Devonshire Fabrics, Inc., 271 F.2d 402, 410 (2d Cir. 1959)).

[110] Gavlik Constr. Co. v. H.F. Campbell Co., 526 F.2d 777, 783 (3d Cir. 1975), *abrogated by* Zosky v. Boyer, 856 F.2d 554 (3d Cir. 1988).

[111] *See* Carolina Throwing Co. v. S & E Novelty Corp., 442 F.2d 329, 331 (4th Cir. 1971) (describing the "modern rule" as a "liberal national policy favoring arbitration").

[112] Shinto Shipping Co. v. Fibrex & Shipping Co., 572 F.2d 1328, 1330 (9th Cir. 1978) (citing Carcich v. Rederi A/B Nordie, 389 F.2d 692, 696 (2d Cir. 1968)).

[113] Belke v. Merrill Lynch, Pierce, Fenner & Smith, 693 F.2d 1023, 1025 (11th Cir. 1982) *abrogated by* Dean Witter Reynolds, Inc. v. Byrd, 470 U.S. 213 (1985).

[114] *See, e.g.*, *Shinto Shipping* at 1330.

[115] *See, e.g.*, Erdman Co. v. Phoenix Land & Acquisition, LLC, 650 F.3d 1115, 1120 n.4 (8th Cir. 2011) ("We can trace the origins of our prejudice requirement to *Carcich v. Rederi A/B Nordie*, 389 F.2d 692, 696 (2d Cir.1968)."); *see also* Gavlik Construction Co. v. H.F. Campbell Co., 526 F.2d 777, 783 (3d Cir. 1975) (citing *Carcich*); Hilti, Inc. v. Oldach, 392 F.2d 368, 371 (1st Cir. 1968) (citing Robert Lawrence Co. v. Devonshire Fabrics, Inc., 271 F.2d 402, 410 (2d Cir. 1959)).

[116] Kulukundis Shipping Co., S/A v. Amtorg Trading Corp., 126 F.2d 978 (1942).

judicial posture and answered Congress's call to end American courts' historical unwillingness to enforce arbitration agreements.

Kulukundis involved a suit in admiralty between two companies to a maritime contract. One issue before the court was whether one party had waived its right to arbitrate.[117] The party resisting arbitration argued that the party seeking arbitration had waived its right to arbitrate because the party seeking arbitration had "contested the existence of the [contract] which contained" the arbitration clause.[118] The Second Circuit rejected this argument and sent the case to arbitration.[119] The Second Circuit was aware of the history of arbitration and acknowledged the judicial hostility to arbitration that American courts had inherited through the common law.[120] The court noted that the FAA was a countermeasure to this historical hostility,[121] and acknowledged the duty of the courts to abide by Congress's efforts to rescue the courts from the old hostility towards arbitration.[122] The court fulfilled its duty by abandoning the English precedent and moving forward with a "new orientation"[123]—one that did not "narrowly construe[]" arbitration agreements.[124]

Duly applying this new orientation, the Second Circuit held that the defendant did not waive its arbitral rights merely because it may have breached the contract.[125] Even so, the court said in dicta that a plaintiff that sued under a contract could not, after a long delay, ask the court to stay proceedings pending arbitration.[126] "Within limits, much might perhaps be said for such a holding, on the ground that a party should not thus first set in motion judicial

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117 *Id.* at 989 (citing 9 U.S.C. § 3 (2012)).

118 *Id.* at 988.

119 *See id.* ("We see no reason why a respondent should be precluded from [] pleading in the alternative.").

120 *See id.* at 982 ("In considering these contentions in the light of the precedents, it is necessary to take into account the history of the judicial attitude towards arbitration . . . .").

121 *See id.* at 985 ("The purpose of that Act was deliberately to alter the judicial atmosphere previously existing.").

122 *Id.* ("In the light of the clear intention of Congress, it is our obligation to shake off the old judicial hostility to arbitration.").

123 *Id.* at 985.

124 *Id.*

125 *Id.* at 989 (citing Shanferoke Coal & Supply Corp. v. Westchester Serv. Corp., 70 F.2d 297 (2d Cir. 1934)).

126 *Id.*

proceedings and then arrest them."[127] The circuit used one notable example of improper conduct—"if the plaintiff wants to avail himself of provision remedies not available in aid of the arbitration."[128] But that was not the case in *Kulukundis*, so the court found no waiver: "[T]he defendant . . . was not in default within the meaning of the proviso in Section 3 [of the FAA]."[129]

By 1968, the Second Circuit had explicitly recognized "an overriding federal policy favoring arbitration" in *Carcich*.[130] The circuit relied on that policy in justifying a no-waiver finding in a case where a defendant (Cunard) had moved to arbitrate.[131] The circuit's language solidified the reasoning that other courts have followed to this day:

> Appellees argue that Cunard should have moved earlier for the stay, and that it delayed for two years in order to be 'in on' the longshoreman's suit. They insist that Cunard has acted inconsistently—it cannot 'have it both ways.' But this argument misses the mark. It is not 'inconsistency,' but the presence or absence of *prejudice* which is determinative of the issue . . . . [I]t may appear that it is inconsistent for a party to participate in a lawsuit for breach of a contract, and later to ask the court to stay that litigation pending arbitration. Yet the law is clear that such participation, standing alone, does not constitute a waiver . . . , for there is an overriding federal policy favoring arbitration. Waiver, therefore, is not to be lightly inferred, and mere delay in seeking a stay of the proceedings without some resultant prejudice to a party . . . cannot carry the day.[132]

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[127] *Id.*

[128] *Id.* at 989 n.40.

[129] *Id.* at 989 (alteration added). Section 3 of the FAA allows courts to grant a stay of litigation pending arbitration, provided the party moving for arbitration is not "in default." *See* 9 U.S.C. § 3 (2012).

[130] Carcich v. Rederi A/B Nordie, 389 F.2d 692, 696 (2d Cir. 1968).

[131] *Id.* (noting the overriding federal policy favoring arbitration).

[132] *Id.* at 696 (emphasis added) (citing *Kulukundis*).

Carcich is therefore an early example of a court's reconciling the FAA with a party's unwillingness to arbitrate. The clash between the FAA's enforcement regime and a party's desire to arbitrate makes sense. The policy favoring arbitration and discussions of arbitration waiver are natural companions. When considering a waiver allegation, courts must determine whether equity would allow arbitration to take place. Congress's elevation of arbitration agreements to a status equivalent to that of other agreements meant that courts were required to give due weight to freely contracted arbitration clauses.

2. Policy and Prejudice

The Second Circuit's decision in *Carcich* to require prejudice, rather than to find waiver based on a party's acts inconsistent with the right to arbitrate, influenced the eventual development of arbitration waiver rules among the circuits. When the Second Circuit refused to find waiver absent prejudice to the party resisting arbitration, it detached the federal policy favoring arbitration from the FAA's core purposes of saving costs, freeing up dockets, and injecting experts into disputes.

Simple waiver and prejudice are critically different analyses. Waiver asks whether a party that wants to arbitrate has acted inconsistently with its right to arbitrate. Courts that focus on waiver (without asking about prejudice to the to the other party) are scrutinizing the party that is most likely to duplicate costs: the moving party. Asking whether those acts caused the *nonmoving* party prejudice shifts a court's focus from the movant's actions to the effects of those actions. This shift is misguided because a party can substantially waste the court's resources without obviously prejudicing its opposing party.[133] A party can also "test the waters" in court without inflicting obvious prejudice. This shift of focus from the acts of the movant to the effects of those acts on the nonmovant came with the federal policy in favor of arbitration.[134]

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[133] *See* Gray Holdco, Inc. v. Cassady, 654 F.3d 444, 454 (3d Cir. 2011) ("[I]n addition to addressing . . . whether the non-moving party suffers prejudice . . . , a court, by finding that there has been a waiver . . . effectuates the principle that a party may not use arbitration to manipulate the legal process and in that process waste scarce judicial resources.").

[134] *Carcich*, 389 F.2d at 696 ("Yet the law is clear that such participation, standing alone, does not constitute a waiver . . . , for there is an overriding federal policy favoring arbitration.").

The natural place for the courts to turn would have been to the principles of equity. Indeed, that seems to have been the Second Circuit's impulse in *Kulukundis* when it said that "a party should not thus first set in motion judicial proceedings and then arrest them."[135] Later courts have similarly taken up equitable principles to determine whether arbitration has been waived when they have discussed issues like whether a party has acted inconsistently with its right to arbitrate, or whether it has manifested an intention contrary to its right to arbitrate.[136] That analysis is consistent with common-law waiver.[137]

But in the context of arbitration waiver, courts have given greater weight to arbitration clauses than the common-law principles of equity demand. The majority of circuits have required not only that a party manifest an intention contrary to its right to arbitrate, but, further, that the party's efforts in litigation are prejudicial to its adversary.[138] The party resisting arbitration often bears the burden of proving that prejudice.[139]

This requirement of prejudice shows a clear preference for arbitration, but it is not entirely consistent with Congress's hopes for the FAA.[140] A rule requiring prejudice to find waiver is a step too far. This rule may result in a situation where a party is asked to participate in litigation and spends considerable time and money doing so but must still arbitrate because it cannot prove sufficient prejudice. In *Carcich*, the court would not find waiver with mere delay, but it recognized the inequity of letting a party "have it both ways."[141] But circuits that require prejudice do, in fact, allow parties to have it both ways.

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135 Kulukundis Shipping Co. v. Amtorg Trading Corp., 126 F.2d 978, 989 (2d Cir. 1942).

136 *See infra* Part III.

137 *See* 13 WILLISTON ON CONTRACTS § 39:28 (4th ed. 2018) (West) ("[A] true waiver, implied from a party's conduct, is dependent solely on what the party charged with waiver intends to do, and there is no need to show reliance by the party asserting or claiming the waiver.").

138 *See, e.g.*, Thyssen, Inc. v. Calypso Shipping Corp., 310 F.3d 102, 105 (2d Cir. 2002) ("The key to a waiver analysis is prejudice."); *see also infra* Part III.

139 *See, e.g.*, Wheeling Hosp., Inc. v. Health Plan, 683 F.3d 577, 586 (4th Cir. 2012) ("The heavy burden of showing default lies with the party opposing arbitration." (internal quotation marks omitted) (quoting Forrester v. Penn Lyon Homes, Inc., 553 F.3d 340, 343 (4th Cir. 2009))).

140 *See supra* Part II.B.

141 Carcich v. Rederi A/B Nordie, 389 F.2d 692, 696 (2d Cir. 1968).

III. THE CIRCUIT VIEWS ON PREJUDICE

Because the Supreme Court has not weighed in on whether a showing of prejudice is required to prove that a party has waived arbitration,[142] this discussion primarily focuses on the status of prejudice in the circuits. Based on the enduring strong federal policy favoring arbitration,[143] the prevailing rule in the circuits is that courts must determine whether there has been prejudice before finding arbitration waiver.[144] There are three exceptions—the Seventh, Tenth, and D.C. Circuits[145]—and the First Circuit requirement of prejudice is "tame at best."[146] A circuit split persists.

A brief survey of the circuits' prejudice rules shows a jurisprudential patchwork. Professor Thomas J. Lilly has organized this patchwork into categories based on the degree of prejudice that circuits require before finding waiver: circuits that impose a "heavy burden" to show prejudice; the First Circuit's "modicum of prejudice" standard; circuits between a "modicum" standard and a "heavy burden" standard; and circuits that require no showing of prejudice at all.[147] This Note roughly follows Professor Lilly's organization but reorganizes the circuits into descending degrees of prejudicial requirements and adds decisions that post-date his 2013 work.

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[142] The Supreme Court granted *certiorari* in one Eleventh Circuit case, *see* Stok & Assocs., P.A. v. Citibank, N.A., 562 U.S. 1215 (2011), but the parties agreed to dismiss the case. *See* 563 U.S. 1029 (2011).

[143] *See* Lilly, *supra* note 28, at 102 ("Those circuits that require a showing of prejudice before there can be a finding of waiver of the right to arbitrate state they do so because of the strong federal policy favoring arbitration.").

[144] *See, e.g.*, MicroStrategy, Inc. v. Lauricia, 268 F.3d 244, 250 (4th Cir. 2001) (finding no waiver, despite the movant's filing three separate actions, delaying six months between the time of the first action and invoking arbitration, and filing more than 50 motions, responses, and other procedural maneuvers).

[145] *See* Thomas J. Lilly, Jr., *Participation in Litigation as a Waiver of the Contractual Right to Arbitrate: Toward a Unified Theory*, 92 NEB. L. REV. 86, 107 (2013) (describing these as circuits that do not require prejudice).

[146] Joca-Roca Real Estate, LLC v. Brennan, 772 F.3d 945, 949 (1st Cir. 2014).

[147] *See* Lilly, *supra* note 145, at 86.

A. PREJUDICE CIRCUITS

Professor Lilly designated the Fourth, Fifth, and Ninth circuits as imposing a heavy burden.[148] The Fourth Circuit's most strenuous requirement of "actual prejudice" still stands as the high watermark.[149] The nonmoving hospital in *Wheeling Hospital, Inc. v. Health Plan of the Upper Ohio Valley, Inc.*, a 2012 Fourth Circuit case, had to respond to two dispositive motions, participate in oral argument, and spend $250,000 in legal fees.[150] Even so, the circuit concluded that "the hospital plaintiffs [] failed to meet their burden of showing [] prejudice."[151] The costs that the hospital suffered in *Wheeling* were exactly the kinds of costs that arbitration is supposed to save. The Fourth Circuit shows no sign of relenting from this heavy burden, which undermines the cost-saving orientation of the FAA.[152]

The strong presumption persists in the Fifth Circuit too,[153] though at least one case indicates that it may be wavering.[154] Older Fifth Circuit rules required substantial prejudice before finding that arbitration had been waived. In *Tenneco Resins, Inc. v. Davy International, AG*, for example, the court found no waiver where the moving party "waited almost eight months before moving [for a stay] pending arbitration, and, in the meantime, participated in

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[148] *Id.* at 103.

[149] *See* Wheeling Hosp., Inc. v. Health Plan of the Upper Ohio Valley, Inc., 683 F.3d 577, 588 (4th Cir. 2012) ("[W]e must determine whether the hospital plaintiffs suffered actual prejudice . . . .").

[150] *Id.* at 583.

[151] *Id.* at 591.

[152] *See also* Patten Grading & Paving, Inc. v. Skanska USA Bldg., Inc., 380 F.3d 200, 208 (4th Cir. 2004) ("With regard to pre-trial litigation expenses, we note that at least one circuit has concluded that incurring the legal expenses inherent in litigation is, without more, 'insufficient evidence of prejudice to justify a finding of waiver.'" (citing *PPG Indus., Inc. v. Webster Auto Parts, Inc.,* 128 F.3d 103, 107 (2d Cir. 1997))).

[153] *See* Joseph Chris Pers. Servs. Inc. v. Rossi, 249 F. App'x 988, 990 (5th Cir. 2007) (adopting the presumption).

[154] *See* Nicholas v. KBR, Inc., 565 F.3d 904, 908 (5th Cir. 2009) (requiring a showing of prejudice, unlike the Seventh Circuit, but finding that "the act of a plaintiff filing suit without asserting an arbitration clause constitutes substantial invocation of the judicial process, unless an exception applies"). An older standard in the Fifth Circuit, like the Fourth, showed a much lower tolerance for acts inconsistent with the right to arbitrate than did its later opinions. *See* Burton-Dixie Corp. v. Timothy McCarthy Const. Co., 436 F.2d 405, 408 (5th Cir. 1971) ("Any conduct of the parties inconsistent with the notion that they treated the arbitration provision in effect . . . may amount to a waiver.").

discovery."[155] The *Tenneco Resins* court also rejected as indicative of prejudice the nonmoving party's "time and expensive of preparing for trial."[156] But the Fifth Circuit may be reevaluating the wasteful prejudice rule. In a more recent case, "the act of a plaintiff filing suit without asserting an arbitration clause constitute[d] a substantial invocation of the judicial process."[157] This language shows at least an awareness of the wastefulness of moving to arbitrate after invoking the judicial process.

Another circuit, the Ninth, recognizes the strong federal policy and the heavy burden on the party resisting arbitration.[158] It requires prejudice in the form of financial costs, duplicitous litigation, or an advantage won from litigation that could not be achieved in arbitration.[159] Still, recognizing that acts inconsistent with an arbitral right can cause duplicative costs,[160] the Ninth Circuit recently found arbitration waiver where seventeen months led to significant pretrial practice.[161] As in the Fifth Circuit, the burden of prejudice in the Ninth Circuit is heavy but may lighten in the future.

The next group of circuits are those that require prejudice before finding that arbitration has been waived, but they do not necessarily require a "heavy burden"—that is, a clear showing of time and money spent in litigation. This Note has already discussed the invocation of the strong federal policy favoring arbitration in the Second Circuit, and noted that wherever that policy rears its head, the burden of prejudice on the party resisting arbitration will likely follow.[162] In the Second Circuit, the prejudice burden is alive and

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155 Tenneco Resins, Inc. v. Davy Int'l, AG, 770 F.2d 416, 420 (1985).

156 *Id.* at 421. In part, the court in that case found no waiver because the moving party had moved to dismiss the action from the outset "because the dispute was covered by a valid and enforceable arbitration clause." *Id.* at 420.

157 *See Nicholas v. KBR*, 565 F.3d at 908.

158 Martin v. Yasuda, 829 F.3d 1118, 1124 (9th Cir. 2016).

159 *Id.* 1126–27.

160 *Id.* at 1127 ("When a party has expended considerable time and money due to the opposing party's failure to timely move for arbitration and is then deprived of the benefits for which it has paid by a belated motion to compel, the party is indeed prejudiced.").

161 *Id.* at 1127–28.

162 *See supra* Part II.

well.[163] The Sixth,[164] Eighth,[165] and Eleventh[166] Circuits have similar standards to that of the Second. Courts in these circuits require prejudice, but parties do not bear the heavy, dollars-and-cents burden that parties bear in the Fourth, Fifth, and Ninth Circuits.

The Third Circuit has developed its own standard. There, a court *may* refuse to enforce an agreement to arbitrate where the movant has acted inconsistently with its right to arbitrate, and the court *will not hesitate* to find waiver where there is prejudice.[167] This rule is similar to the two-tier rule that I suggest. The Third Circuit gives district courts some discretion where a party has acted inconsistently with its right to arbitrate before moving to arbitrate.[168] This makes sense. A party might have good reason not to move to arbitrate right away. There may be some doubt about the arbitrability of the claim, for example. But where the nonmoving party show prejudice, the circuit "will not hesitate to hold that the right to arbitrate has been waived."[169] This also makes sense.

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[163] LG Elec., Inc. v. Wi-Lan USA, Inc., 623 F. App'x 568, 569 (2d Cir. 2015) ("[W]aiver 'may be found only when prejudice to other party is demonstrated.'" (quoting Thyssen, Inc. v. Calypso Shipping Corp., 310 F.3d 102, 105 (2d Cir. 2002)); Etransmedia Tech., Inc. v. Nephrology Assocs., P.C., No. 1:11–CV–1042, 2013 WL 1105440, at *3 (N.D.N.Y. Mar. 18, 2013) (citing factors, including proof of prejudice, from La. Stadium & Exposition Dist. v. Merrill Lynch, Pierce, Fenner & Smith Inc., 626 F.3d 156, 159 (2d Cir. 2010)).

[164] *See, e.g.*, Hurley v. Deutsche Bank Tr. Co. Am., 610 F.3d 334, 338 (6th Cir. 2010) (holding that a party may waive its arbitral rights by engaging in two courses of conduct: (1) acting inconsistently with the right to arbitrate and (2) causing prejudice by its delay in invoking arbitration); *see also* Shy v. Navistar Int'l Corp, 781 F.3d 820, 828 (6th Cir. 2015) ("Both inconsistency and actual prejudice are required, and neither is present here.").

[165] In 2011, the Eighth Circuit noted the "controversial" nature of the prejudice issue. Erdman Co. v. Phoenix Land & Acquisition, LLC, 650 F.3d 1115, 1118 (8th Cir. 2011). The circuit applied the prejudice burden but said that the question whether inconsistent acts amounted to prejudice should be determined on a case-by-case basis, citing the Seventh Circuit for the tenuousness of its prejudice requirement. *Id.* at 1119.

[166] *See, e.g.*, Grigsby & Assocs., Inc. v. M Sec. Inv., 635 F. App'x 728, 731–33 (11th Cir. 2015) (applying the strong federal policy and finding no waiver despite 10 years' delay, because three of the four lawsuits movant filed in that time were insubstantial, and the movant's malpractice suit against its former counsel was irrelevant); Garcia v. Wachovia Corp., 699 F.3d 1273, 1276 (11th Cir. 2012) (requiring prejudice but finding waiver where parties served and answered interrogatories, produced approximately 900,000 pages of discovery documents, and took approximately 20 depositions).

[167] In re Pharmacy Benefit Managers Antitrust Litig., 700 F.3d 109, 117 (3d Cir. 2012).

[168] *See id.* at 117 ("A court may, however, refuse to enforce an arbitration agreement where a party has acted inconsistently with the right to arbitrate . . . .") (internal quotation marks omitted).

[169] *Id.*

Prejudice is a bellwether of wasteful litigation. If one party has litigated to the point that the other party has suffered costs in time, energy, or prejudice to their legal position, that is a strong sign that the moving party has abused the alternative venue system. The Third Circuit considers a handful of factors from its opinion in *Hoxworth v. Blinder, Robinson & Co.*, 980 F.2d 912 (3d Cir. 1992) to determine whether a party has suffered prejudice.[170] Notably, the Third Circuit standard aligns closely with that of the Seventh Circuit and its presumptive waiver rule, which reflects a drift from its earlier position between the heavy burden circuits and the First Circuit's modicum standard.[171]

The First Circuit's prejudice requirement is "tame at best."[172] In this, it is like the Third Circuit; both circuits will find waiver with very little prejudice at all. Also like the Third, the First Circuit applies a "salmagundi of factors, including: the length of the delay, the extent to which the party seeking to invoke arbitration has participated in the litigation, the quantum of discovery and other litigation-related activities that have already taken place, the proximity of the arbitration demand to an anticipated trial date, and the extent to which the party opposing arbitration would be prejudiced."[173]

While it may be premature to tease out a trend from such a pandemonium of circuit jurisprudence, there does seem to be some shift in recent years towards greater vigilance over acts inconsistent with the right to arbitrate. This is clear both from the cracks in the foundation of the heavy-burden circuits—like the Fifth and Ninth—and in the willingness of circuits like the Eighth to acknowledge the danger in finding no waiver where parties have engaged in duplicative litigation. This shift towards no-prejudice approaches the standard in the Seventh Circuit, first expounded in *St. Mary's Medical Center of Evansville, Inc. v. Disco Aluminum Production Co.*, 969 F.2d 585 (7th Cir. 1992).

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[170] *In re Pharmacy Benefit Managers*, 700 F.3d at 117. For a full discussion of the factors that courts consider in determining waiver, see Donald E. Frechette, *Waiving the Right to Arbitrate by Participating in Litigation*, 80 DEF. COUNS. J. 223, 224–28 (2013).

[171] *See* Lilly, *supra* note 145, at 107.

[172] Joca-Roca Real Estate, LLC v. Brennan, 772 F.3d 945, 949 (1st Cir. 2014).

[173] *Id.* at 948.

B. NO-PREJUDICE CIRCUITS

The Seventh Circuit holds that courts "may find waiver absent prejudice," and that the waiver inquiry is one that depends on the totality of the circumstances.[174] The circuit noted in *St. Mary's* that its conclusion was not inconsistent with the strong federal policy favoring arbitration.[175] While Congress intended to put arbitration agreements on the same footing as other contracts,[176] "the federal policy embodied in the Arbitration Act is a policy favoring enforcement of contracts, not a preference for arbitration over litigation."[177] While the history and context in which Congress enacted the FAA to some extent *do* seem to suggest a preference for arbitration, owing to the benefits of speedy resolution and the expertise of an arbitrator, the rule that the Seventh Circuit reached in *St. Mary's* more closely aligns with the spirit of Congress's preference—cost savings and efficiency.

In its later opinions, the Seventh Circuit spelled out the implications of its no-prejudice rule. In *Cabinetree of Wisconsin, Inc. v. Kraftmaid Cabinetry, Inc.*, the Seventh Circuit took the next step, holding that an election to proceed before a nonarbitral tribunal for the resolution of a contractual dispute is a presumptive waiver of the right to arbitrate.[178] The circuit noted that the principal treatise on arbitration supports its rule[179] and that in ordinary contract law, a waiver is normally effective without proof of consideration or detrimental reliance.[180] The court reasoned that an arbitration clause gives a party an alternative choice, but "the intention behind such clauses, and the reason for judicial enforcement of them, are

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[174] *See* St. Mary's Med. Ctr. of Evansville, Inc. v. Disco Aluminum Prod. Co., 969 F.2d 585, 590 (7th Cir. 1992) ("While none of our cases have stated explicitly that a court may find waiver absent prejudice, that principle is implicit in our repeated emphasis that waiver depends on all the circumstances in a particular case rather than on any rigid rules and that prejudice is but one relevant circumstance to consider in determining whether a party has waived its right to arbitrate.").

[175] *Id.*

[176] *Id.* (quoting Dean Whitter Reynolds, Inc. v. Byrd, 470 U.S. 213, 219 (1985)).

[177] *Id.*

[178] Cabinetree of Wis., Inc. v. Kraftmaid Cabinetry, Inc., 50 F.3d 388, 390 (7th Cir. 1995).

[179] *Id.* (citing 2 IAN R. MACNEIL, RICHARD E. SPEIDEL & THOMAS J. STIPANOWICH, FEDERAL ARBITRATION LAW: AGREEMENTS, AWARDS, AND REMEDIES UNDER THE FEDERAL ARBITRATION ACT § 21.3.3 (1994)).

[180] *Id.* (citing E. ALLAN FARNSWORTH, CONTRACTS § 8.5 (2d ed. 1990); 3A ARTHUR L. CORBIN, CORBIN ON CONTRACTS § 753 (1960)).

not to allow or encourage the parties to proceed, either simultaneously or sequentially, in multiple forums."[181]

However, the Seventh Circuit also noted some exceptions. Judge Posner explained that situations might arise where invocation of the judicial process does not signify an intention to proceed in a court to the exclusion of arbitration.[182] A party might have doubts about arbitrability but face the prospect of a statute of limitations running; it might sue where some issues are arbitrable and others are not; or some unexpected development might arise in discovery that justifies a resort to arbitration.[183] Other courts have observed that a party might sue "solely to obtain a threshold declaration as to whether a valid arbitration agreement existed," or "to obtain injunctive relief pending arbitration."[184]

IV. ANALYSIS AND CONCLUSION

In upholding the federal policy favoring arbitration, the courts were doing their part to advance the same goals that Congress had when it passed the FAA. It stands to reason, then, that courts should enforce arbitration when doing so is consistent with the goals of the FAA—cost savings, alleviating court clogs, and introducing an expert arbitrator. But when a rule favoring arbitration duplicates costs or contributes to delays in adjudication, courts should decline to invoke the federal policy favoring arbitration. Without the efficiency benefits, the federal policy favoring arbitration is meaningless and counterproductive.

Of the prevailing rules, the Seventh Circuit's most aggressively enforces the efficiency-related purposes of the FAA. Congress introduced the FAA to save on costs of litigation, alleviate court clogs, and utilize an expert arbitrator in disputes. Allowing parties to proceed with litigation before they invoke their arbitral rights poses a serious threat of duplicative litigation costs and clogs court dockets. So the prevailing rule among the circuits, which calls for a showing of at least some prejudice to the nonmovant before finding

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[181] *Id.*

[182] *Id.* ("[I]t is easy to imagine situations . . . in which such invocation does not signify an intention to proceed in a court to the exclusion of arbitration.").

[183] *Id.* at 391 (enumerating possibilities and noting that they are not exhaustive).

[184] Nicholas v. KBR, Inc., 565 F.3d 904, 908–09 (5th Cir. 2009).

that arbitration has been waived, is *per se* wasteful. A rule like the Seventh Circuit's instead prevents gamesmanship because a party cannot try its luck in a judicial forum and then invoke arbitration when things go poorly, inflicting the resultant procedural costs on the judicial system.[185]

But the *Cabinetree* rule—that a decision to proceed before a nonarbitral tribunal raises a presumption of waiver—is too strong. In a case that followed *Cabinetree*, the Seventh Circuit cabined its doctrine, finding that a response does not raise a presumption of waiver.[186] This is only fair, since a party at such an early stage should not have to run the risk of a default judgment while it decides whether to litigate or arbitrate.[187]

Consistent with the underlying purposes of the FAA, and to prevent litigative gamesmanship, courts should apply a two-tiered analysis. Under the first tier, courts should automatically find waiver where a party deliberately manipulates the judicial process or gains an advantage it would not have gained in arbitration. For example, a party might take advantage of courts' broad discovery rules to win a smoking-gun document, only to move for arbitration once the party obtained the document. Under the second tier, courts should rebuttably presume waiver where a party duplicates the machinery of arbitration by litigating in court. This standard will best ensure that the cost-saving function of the FAA is vindicated, while giving parties an equitable outlet when they litigate in good faith. A party might need to fend off an aggressor in litigation while it weighs its options, or the party might have genuine doubts about the arbitrability of its claim but need to file to meet a statute of limitations. A party's change in counsel could cut either way.

Of course, it is possible that the savings to the parties of arbitration would be so great that, even where some costs are duplicated by unnecessary litigation, arbitration would still result in a net-savings to the parties and the judiciary. Still, if one party has resisted a motion to compel arbitration, that resistance

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185 *See generally* Lilly, *supra* note 145 (agreeing with the Seventh Circuit and arguing that courts should rebuttably presume waiver where litigants fail to raise arbitration as a defense at the pleading stage).

186 Kawasaki Heavy Indus., Ltd. v. Bombardier Recreational Prod., Inc., 660 F.3d 988, 995 (7th Cir. 2011).

187 *See id.* at 996 (noting that a party's failure to participate in an appeal or mediation would have caused a default judgment in the other party's favor).

probably shows that it expects litigation to provide the most value. Asking a court to assess the savings to the parties by invoking arbitration asks too much. Courts are in a better position to provide a prophylactic rule that ensures parties will invoke their arbitral rights at the earliest possible moment or be bound by their decision to litigate.

To litigate with arbitration as a fallback is "like testing the water before taking the swim. If it's not to your liking you go elsewhere."[188] But litigating with arbitration as a fallback is not just an unfair benefit to the party seeking arbitration; it also costs courts and opposing parties who must entertain the litigation. Taxing courts and parties in this way runs counter to the animating purposes of the FAA—saving costs, clearing dockets, and inviting experts into disputes. Courts should reconsider the burden of prejudice that nonmovants must bear to show that arbitration has been waived. Instead, courts should find waiver where a party deliberately plays the two-venue system or wins an unfair advantage in litigation. Courts should rebuttably presume waiver where a party's conduct shows intent to litigate. This rule would put courts on high alert for parties trying to have it both ways.

[188] McConnell v. Merrill Lynch, Inc., 164 Cal. Rptr. 751, 754 (Cal. Ct. App. 1980).